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# GILCHRIST HOSPICE CARE, INC. AND SUBSIDIARIES D/B/A GILCHRIST SERVICES, INC.

Consolidated Financial Statements
and Consolidating Information

June 30, 2016 and 2015

(With Independent Auditors' Report Thereon)

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

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KPMG LLP
1 East Pratt Street
Baltimore, MD 21202-1128

## Independent Auditors' Report

The Board of Directors
Gilchrist Hospice Care, Inc.:

We have audited the accompanying consolidated financial statements of Gilchrist Hospice Care, Inc. and its subsidiaries d/b/a Gilchrist Services, Inc. (the Hospice), which comprise the consolidated balance sheets as of June 30, 2016 and 2015, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditors' Responsibility*

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### *Opinion*

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Gilchrist Hospice Care, Inc. and its subsidiaries d/b/a Gilchrist Services, Inc. as of June 30, 2016 and 2015, and the results of their operations and their cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

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***Other Matter***

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying supplementary information in Schedules 1–2 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

October 6, 2016

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

Consolidated Balance Sheets

June 30, 2016 and 2015

(In thousands)

| **Assets** | | **2016** | **2015** |
|---|---|---|---|
| Current assets: | | | |
| Cash and cash equivalents | $ | 10,625 | 7,364 |
| Limited or restricted use funds | | 2,460 | 1,771 |
| Patient accounts receivable, net of reserves of $1,747 and $2,956 | | 5,932 | 7,710 |
| Other receivables | | 549 | 713 |
| Inventories and prepaid expenses | | 114 | 242 |
| Current pledge receivables | | 1,238 | 500 |
| Total current assets | | 20,918 | 18,300 |
| Noncurrent assets: | | | |
| Investments and limited or restricted use funds | | 79,744 | 80,314 |
| Pledge receivables, net | | 2,084 | 1,084 |
| Property, plant and equipment, net | | 12,691 | 12,203 |
| Other assets | | 284 | 299 |
| Total noncurrent assets | | 94,803 | 93,900 |
| Total assets | $ | 115,721 | 112,200 |
| **Liabilities and Net Assets** | | | |
| Current liabilities: | | | |
| Accounts payable and accrued expenses | $ | 5,174 | 4,091 |
| Insurance reserves, current | | 150 | 228 |
| Current portion of long-term debt | | — | 489 |
| Advances from affiliates | | 762 | 932 |
| Other current liabilities | | 478 | 356 |
| Total current liabilities | | 6,564 | 6,096 |
| Noncurrent liabilities: | | | |
| Long-term debt | | — | 777 |
| Insurance reserves | | 274 | 247 |
| Other long-term liabilities | | 615 | 615 |
| Total liabilities | | 7,453 | 7,735 |
| Net assets: | | | |
| Unrestricted | | 85,665 | 83,209 |
| Temporarily restricted | | 8,392 | 7,074 |
| Permanently restricted | | 14,211 | 14,182 |
| Total net assets | | 108,268 | 104,465 |
| Total liabilities and net assets | $ | 115,721 | 112,200 |

See accompanying notes to consolidated financial statements.

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

Consolidated Statements of Operations

Years ended June 30, 2016 and 2015

(In thousands)

| | | 2016 | 2015 |
|---|---|---|---|
| Patient service revenue: | | | |
| Patient service revenue, net of contractual allowances | $ | 48,380 | 41,391 |
| Provision for uncollectible accounts | | (1,656) | (1,751) |
| Net patient service revenue | | 46,724 | 39,640 |
| Other operating revenue: | | | |
| Other revenue | | 157 | 90 |
| Net assets released from restrictions | | 3,547 | 3,519 |
| Total operating revenue | | 50,428 | 43,249 |
| Operating expenses: | | | |
| Salaries, wages and employee benefits | | 33,022 | 30,451 |
| Expendable supplies | | 3,889 | 2,971 |
| Purchased services | | 8,938 | 7,547 |
| Depreciation | | 1,358 | 1,268 |
| Interest | | 31 | 40 |
| Total operating expenses | | 47,238 | 42,277 |
| Total operating income | | 3,190 | 972 |
| Other income (expense): | | | |
| Contributions | | 685 | 708 |
| Fund-raising expense | | (968) | (1,003) |
| Investment (loss) income, net | | (451) | 2,908 |
| Inherent contribution | | — | 1,357 |
| Total other (loss) income | | (734) | 3,970 |
| Excess of revenues over expenses | $ | 2,456 | 4,942 |

See accompanying notes to consolidated financial statements.

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

Consolidated Statements of Changes in Net Assets

Years ended June 30, 2016 and 2015

(In thousands)

| | | 2016 | 2015 |
|---|---|---|---|
| Excess of revenues over expenses and changes in unrestricted net assets | $ | 2,456 | 4,942 |
| Changes in temporarily restricted net assets: | | | |
| Contributions | | 5,279 | 2,947 |
| Investment (loss) income, net | | (414) | 24 |
| Net assets released for operations | | (3,547) | (3,519) |
| Inherent contribution | | — | 31 |
| Increase (decrease) in temporarily restricted net assets | | 1,318 | (517) |
| Changes in permanently restricted net assets: | | | |
| Contributions | | 140 | 286 |
| Investment loss, net | | (111) | (89) |
| Inherent contribution | | — | 2,322 |
| Increase in permanently restricted net assets | | 29 | 2,519 |
| Increase in net assets | | 3,803 | 6,944 |
| Net assets, beginning of year | | 104,465 | 97,521 |
| Net assets, end of year | $ | 108,268 | 104,465 |

See accompanying notes to consolidated financial statements.

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

Consolidated Statements of Cash Flows

Years ended June 30, 2016 and 2015

(In thousands)

| | | 2016 | 2015 |
|---|---|---|---|
| Cash flows from operating activities: | | | |
| Change in net assets | $ | 3,803 | 6,944 |
| Adjustments to reconcile change in net assets to net cash provided by (used in) operating activities: | | | |
| Depreciation expense | | 1,358 | 1,268 |
| Provision for uncollectible accounts | | 1,656 | 1,751 |
| Realized/unrealized loss (gains) on investments | | 2,614 | (1,330) |
| Restricted interest income on investments | | (272) | (169) |
| Restricted contributions | | (5,419) | (3,233) |
| Inherent contribution related to Joseph Richey acquisition | | — | (3,710) |
| Changes in assets and liabilities: | | | |
| Decrease (increase) in patient accounts receivable | | 122 | (3,541) |
| Decrease in other assets | | 307 | 24 |
| Increase (decrease) in accounts payable and accrued expenses | | 1,154 | (328) |
| Net cash provided by (used in) operating activities | | 5,323 | (2,324) |
| Cash flows from investing activities: | | | |
| Increase in investments and restricted use funds | | (2,461) | (1,963) |
| Additions to property and equipment | | (1,846) | (398) |
| Cash assumed in connection with Joseph Richey House acquisition | | — | 245 |
| Net cash used in investing activities | | (4,307) | (2,116) |
| Cash flows from financing activities: | | | |
| Payment on long-term debt | | (1,266) | (52) |
| Transfer (to) from affiliates | | (170) | 176 |
| Proceeds from restricted contributions | | 3,681 | 3,072 |
| Net cash provided by financing activities | | 2,245 | 3,196 |
| Increase (decrease) in cash | | 3,261 | (1,244) |
| Cash and cash equivalents, beginning of year | | 7,364 | 8,608 |
| Cash and cash equivalents, end of year | $ | 10,625 | 7,364 |
| Cash paid for interest | $ | 23 | 32 |

See accompanying notes to consolidated financial statements.

(In thousands)

## (1) Nature of Operations

Gilchrist Hospice Care, Inc. (the Hospice) is a not-for-profit corporation and a wholly owned subsidiary of GBMC HealthCare, Inc. (the Company). The Hospice, doing business as Gilchrist Services, Inc., provides inpatient and home care hospice services and provides education about hospice care and bereavement services to the public and the healthcare community in Maryland.

***Acquisition of the Joseph Richey House, Inc.***

On October 31, 2014, the Hospice entered into an Affiliation Agreement with Joseph Richey House, Inc. (JRH) and Brownlow Byron Home, Inc (BBH), collectively referred to as Richey, under which the Hospice became the sole member of JRH and BBH. No consideration was tendered in connection with the transaction.

JRH is an inpatient hospice residence for terminally ill persons lacking a caregiver in their own homes. JRH has been serving patients in Baltimore City since 1987, providing residential, acute and respite care. JRH is a not-for-profit organization.

BBH is not-for-profit organization that provides elderly and disable persons with housing facilities services in the Richey facility since 1997.

The affiliation was accounted for under the purchase accounting method for business combinations and the financial position and results of operations for Richey were consolidated by the Hospice beginning on November 1, 2014. The Hospice recognized an inherent contribution equal to the estimated fair value of the identifiable net assets of Richey on the acquisition date of $3,710, of which $1,357 was included in nonoperating income on the consolidated statements of activities and $31 and $2,322 were included as a temporarily restricted and permanently restricted inherent contributions, respectively, and reported in the consolidated statements of changes in net assets.

The following table summarizes the estimated fair value of assets acquired and liabilities assumed at November 1, 2014 (the acquisition date):

| | | |
|---|---|---|
| Assets: | | |
| Current assets | $ | 709 |
| Property and equipment | | 4,002 |
| Other long-term assets | | 2,259 |
| Total assets | $ | 6,970 |
| Liabilities: | | |
| Current liabilities | $ | 1,834 |
| Long-term liabilities | | 1,426 |
| Total liabilities | $ | 3,260 |

(In thousands)

| | | |
|---|---|---|
| Net assets: | | |
| Unrestricted | $ | 1,357 |
| Temporarily restricted | | 31 |
| Permanently restricted | | 2,322 |
| Total net assets | | 3,710 |
| Total liabilities and net assets | $ | 6,970 |

The following table summarizes the Hospice's pro forma consolidated results for the year ended June 30, 2015 as though the acquisition date occurred on July 1, 2014.

| | | **2015** |
|---|---|---|
| Total operating revenue | $ | 44,033 |
| Total operating income | | 275 |
| Changes in net assets: | | |
| Unrestricted | $ | 3,585 |
| Temporarily restricted | | (548) |
| Permanently restricted | | 197 |
| Total change in net assets | $ | 3,234 |

Hospice's consolidated financial statements include JRH and BBH since the organization has both control and economic interest in these entities.

## (2) Summary of Significant Accounting Policies

### *(a) Basis of Accounting*

The accompanying financial statements have been prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles. Significant intercompany accounts and transactions have been eliminated in consolidation.

### *(b) Cash and Cash Equivalents*

Cash and cash equivalents, carried at cost, which approximates fair value, include amounts invested in accounts that are readily convertible to known amounts of cash with original maturities of three months or less. Cash balances may exceed amounts insured by federal agencies and, therefore, bear a risk of loss. Hospice has not experienced such losses on these funds to date.

### (c) *Limited Use Funds*

Limited use funds are designated by the donor for a specific use or purpose. Once the donor restrictions have been met, these funds are then released for operations.

### (d) *Investments and Investment Income*

The Hospice investment portfolio is considered a trading portfolio. Investments in marketable securities are measured at fair value. The fair values of the investments are based on quoted market prices or dealer quotes. See note 4 for the discussion of the measurement for fair value for investments.

Alternative investments are recorded under the equity method of accounting. Underlying securities of these alternative investment may include certain debt and equity securities that are not readily marketable. Because certain investments are not readily marketable, their fair value is subject to additional uncertainty, and therefore, values realized upon disposition may vary significantly from current reported values.

Investment income or loss (including realized gains and losses on investments, interest, and dividends) is included in excess of revenues over expenses unless the income or loss is restricted by the donor or law. Investment income on investments of temporarily restricted or permanently restricted net assets is recorded as an increase or decrease in temporarily restricted net assets to the extent restricted by the donor or law.

Investment income is recorded on the accrual basis. Purchases and sales of investments are reflected on a trade-date basis. Realized gains and losses on sales of investments are based on historical cost.

In May 2005, Hospice received an unrestricted contribution of approximately $25 million to support the ongoing activities of the Hospice. The board of directors of the Hospice has internally designated the contribution for future use.

### (e) *Allowance for Bad Debts*

Patient accounts receivable are reduced by allowances for bad debts. In evaluating the collectibility of accounts receivable, the Hospice analyzes historical collections and write-offs and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for bad debts and provision for uncollectible accounts. Management regularly reviews its estimate and evaluates the sufficiency of the allowance for bad debts. The Hospice analyzes contractual amounts due from patients who have third-party coverage and provides an allowance for doubtful accounts and a provision for bad debts. For patient accounts receivable associated with self-pay patients, which includes those patients without insurance coverage exists for a portion of the bill, the Hospice records a significant provision for bad debts for patients that are unable or unwilling to pay for the portion of the bill representing their financial responsibility. Account balances are charged off against the allowance for doubtful accounts after all means of collection have been exhausted.



(Continued)

(In thousands)

Hospice allowance for doubtful accounts decreased from 27% to 23% of gross accounts receivable from June 30, 2015 to June 30, 2016.

The activity in the allowance for bad debts is summarized as follows for the fiscal years ended June 30:

| | | 2016 | 2015 |
|---|---|---|---|
| Beginning balance | $ | 2,956 | 1,486 |
| Provision for uncollectible accounts | | 1,656 | 1,751 |
| Less write offs | | (2,865) | (281) |
| Ending balance | $ | 1,747 | 2,956 |

### *(f) Ground Lease*

Ground lease represents the prepayment for the lease of land used by the Hospice. The ground lease is being amortized over 40 years, through March 2033, which is the life of the lease. Ground lease expense was $16 for the years ended June 30, 2016 and 2015, and is recorded as purchased services on the consolidated statements of operations. Ground lease prepayments are included in other assets on the consolidated balance sheets.

### *(g) Property, Plant and Equipment*

Property, plant, and equipment are recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, which range from 3 to 36 years. The cost and accumulated depreciation relating to property, plant, and equipment sold or retired are removed from the respective accounts at the time of disposition and the resulting gain or loss is reflected in the consolidated statements of operations.

### *(h) Other Long-Term Liabilities*

Other long-term liabilities consist of a capital advance in the amount of $615 from the U.S. Department of Housing and Urban Development (HUD). The capital advance does not bear any interest and is not required to be repaid as long as the housing remains available to eligible low-income households for a period of 40 years, expiring in 2040, and functions in accordance with Section 811.

### *(i) Donor-Restricted Gifts*

Unconditional promises to give cash and other assets to Hospice are reported at their fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted if they are received with donor stipulations that limit the use of donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose of the restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying consolidated financial statements.

### *(j) Temporarily and Permanently Restricted Net Assets*

Temporarily restricted net assets are those whose use by the Hospice has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Hospice in perpetuity.

Richey is one of six named beneficiaries of a charitable trust and receives annual distributions for 50 years, which began in 2005. The distributions are to be used for the unrestricted general charitable purpose of the Richey. After the 50 years, the trust corpus will be distributed to the charities as long as they continue to qualify as a charitable organization under Sections 171(c) and 2055(a) of the Internal Revenue Code. The corpus must be used to create an endowment fund which is permanently restricted and the income should be used for the organization's unrestricted general charitable purpose. The fair value of the trust is included in permanently restricted net assets.

### *(k) Net Patient Service Revenue*

Net patient service revenue is billed on a per-diem basis based on the Medicare fee schedule and contractual agreements for other third-party payors.

### *(l) Excess of Revenues over Expenses*

The consolidated statements of operations include a performance indicator, excess of revenues over expenses. The changes in unrestricted net assets that are excluded from excess of revenues over expenses, consistent with industry practice, include contributions of long-lived assets, including assets acquired using contributions, which by donor restriction were to be used for the purpose of acquiring such assets.

### *(m) Financial Assistance*

As part of the Hospice's mission, it provides hospice care without discrimination on any grounds, including the patients' ability to pay for services. Patients who meet certain criteria under its charity care policy receive free care or services for which the Hospice accepts payments at less than its established rates.

Because the Hospice does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Based on established rates, the Hospice recorded $340 and $112 of charity care in 2016 and 2015, respectively. The total direct and indirect cost of providing the financial assistance was approximately $221 and $103 in 2016 and 2015, respectively.



(Continued)

### *(n) Income Taxes*

The Hospice is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and is exempt from federal income taxes on related income pursuant to Section 501(a) of the Code.

The Financial Accounting Standards Board's (FASB) guidance on accounting for uncertainty in income taxes clarifies the accounting for uncertainty of income tax positions. This guidance defines the threshold for recognizing tax return positions in the financial statements as "more likely than not" that the position is sustainable, based on its technical merits. This standard also provides guidance on the measurement, classification and disclosure of tax return positions in the consolidated financial statements. The Hospice has adopted this guidance, and there were no amounts recorded in the consolidated financial statements during the years ended June 30, 2016 and 2015 for uncertain tax positions.

### *(o) Use of Estimates*

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

### *(p) New Accounting Pronouncements*

The FASB issued Accounting Standards update (ASU) 2014-09, Revenue from Contracts with Customers (Topic 606). This ASU establishes principles for reporting useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from the entity's contracts with customers. Particularly, that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU 2014-09 is effective for fiscal year 2019. Hospice does not anticipate that the adoption of this ASU will have a material impact on its financial position or its results of operations.

The FASB issued ASU No. 2016-02, *Leases (ASU 2016-02)*, which will require lessees to recognize most leases on-balance sheet, which will increase their reported assets and liabilities. The adoption of ASU 2016-02 is effective in fiscal year 2020, and will require application of the new guidance at the beginning of the earliest comparable period presented. Early adoption is permitted. Hospice is currently assessing the impact of the adoption of ASU No. 2016-02 which is expected to increase the Company's assets and liabilities but not have a significant impact on the results of operations.

(In thousands)

The FASB issued ASU No. 2016-14, *Not-for-Profit Entities (ASU 2016-14)*, which amends the requirements for financial statements and notes in Topic 958, Not-for-Profit Entities (NFP), and requires a NFP to:

- Reduce the number of net asset classes presented from three to two: with donor restrictions and without donor restrictions;
- Present expenses by their functional and their natural classifications in one location in the financial statements;
- Provide quantitative and qualitative information about management of liquid resources and availability of financial assets to meet cash needs within one year of the balance sheet date.

The adoption of ASU 2016-14 is effective in fiscal year 2019, and is applied retrospectively in the year of adoption. Hospice does not anticipate that the adoption of this ASU will have a material impact on its financial position and results of operations.

## (3) Concentrations of Credit Risk

The Hospice grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of net patient service revenue and patient accounts receivable from third parties as of and for the years ended June 30 is as follows:

| | Accounts receivable | | Revenue | |
|---|---|---|---|---|
| | **2016** | **2015** | **2016** | **2015** |
| Medicare | 66% | 52% | 86% | 83% |
| Medicaid | 4 | 4 | 3 | 3 |
| Blue Cross | 6 | 13 | 1 | 1 |
| Commercial managed care entities | 8 | 15 | 6 | 7 |
| Other third party payors | 16 | 16 | 4 | 6 |
| Total | 100% | 100% | 100% | 100% |

Hospice provides hospice services in the state of Maryland. Hospice and other healthcare providers are subject to certain inherent risks, including: dependence on revenues derived from reimbursement by the federal Medicare and state Medicaid programs, and government regulation, government budgetary constraints, and proposed legislative and regulatory changes.

The Medicare and state Medicaid reimbursement programs represent a substantial portion of the Hospice's revenues and the Hospice's operations are subject to a variety of other federal, state, and local regulatory requirements. Failure to maintain required regulatory approvals and licenses and/or changes in such regulatory requirements could have a significant adverse effect on the Hospice. Changes in federal and state reimbursement funding mechanisms and related government budgetary constraints could have a significant adverse effect on the Hospice.

As a result of recently enacted and pending federal healthcare reform legislation, substantial changes are anticipated in the U.S. healthcare system. Such legislation includes numerous provisions affecting the delivery of healthcare services, the financing of healthcare costs, reimbursement to healthcare providers, and the legal obligations of health insurers, providers, and employers. These provisions are currently slated to take effect at specified times over the next decade. This federal healthcare reform legislation did not affect the 2016 and 2015 consolidated financial statements.

Additional Documentation Requests or (ADR) began in December 2009 to perform prepayment reviews of claims targeted to those services with the highest improper payments. ADR reviews at the Hospice covered areas of beneficiary election statement, certification, plans of care and eligibility.

## (4) Investments and Limited Use Funds

Guidance for fair value measurements establishes a hierarchy of valuation inputs based on the extent to which the inputs are observable in the marketplace. Observable inputs reflect market data obtained from sources independent of the reporting entity and unobservable inputs reflect the entities own assumptions about how market participants would value an asset or liability based on the best information available. Valuation techniques used to measure fair value under current guidance must maximize the use of observable inputs and minimize the use of unobservable inputs. The guidance describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value.

The following describes the hierarchy of inputs used to measure fair value and the primary valuation methodologies used by the Hospice for financial instruments measured at fair value on a recurring basis. The three levels of inputs are as follows:

- Level 1 – Quoted prices in active markets for identical assets or liabilities
- Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the same term of the assets or liabilities
- Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

(In thousands)

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The tables below presents the balances of assets measured at fair value by level excluding alternative investments in the amount of $356 and $327, which are accounted for under the equity method, as of June 30, 2016 and 2015, respectively:

| | June 30, 2016 | | | |
|---|---|---|---|---|
| | **Level 1** | **Level 2** | **Level 3** | **Total** |
| Managed cash funds | $ 4,035 | — | — | 4,035 |
| Corporate debt securities | — | 2,455 | — | 2,455 |
| Bonds – treasury | 134 | — | — | 134 |
| Bonds – federal agency backed | — | 96 | — | 96 |
| Bonds – fixed income | — | 474 | — | 474 |
| Bonds – fixed income international | — | 52 | — | 52 |
| Mutual funds – fixed income | — | 22,511 | — | 22,511 |
| Municipal bonds | — | 126 | — | 126 |
| Total fixed income | 134 | 25,714 | — | 25,848 |
| Common stock | 39,299 | 58 | 232 | 39,589 |
| Foreign stock | 3,241 | — | — | 3,241 |
| Mutual funds | 9,135 | — | — | 9,135 |
| Total equity | 51,675 | 58 | 232 | 51,965 |
| Total investment and limited or restricted use funds | 55,844 | 25,772 | 232 | 81,848 |
| Less current portion | 2,460 | — | — | 2,460 |
| Total noncurrent investment and limited or restricted use funds | $ 53,384 | 25,772 | 232 | 79,388 |

(In thousands)

| | June 30, 2015 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| Managed cash funds | $ 5,799 | — | — | 5,799 |
| Corporate debt securities | — | 5,662 | — | 5,662 |
| Bonds – fixed income | — | 387 | — | 387 |
| Bonds – fixed income international | — | 77 | — | 77 |
| Mutual funds – fixed income | — | 18,589 | — | 18,589 |
| Municipal bonds | — | 155 | — | 155 |
| Total fixed income | — | 24,870 | — | 24,870 |
| Common stock | 37,793 | — | 258 | 38,051 |
| Foreign stock | 3,767 | — | — | 3,767 |
| Mutual funds | 9,271 | — | — | 9,271 |
| Total equity | 50,831 | — | 258 | 51,089 |
| Total investment and limited or restricted use funds | 56,630 | 24,870 | 258 | 81,758 |
| Less current portion | 1,771 | — | — | 1,771 |
| Total noncurrent investment and limited or restricted use funds | $ 54,859 | 24,870 | 258 | 79,987 |

Hospice values Level 1 marketable securities using the closing market prices as of the valuation date. Fair values determined by Level 1 inputs utilize quoted trades at least weekly in an active market. The Hospice values Level 2 investments using the current prices published. Fair values determined by Level 2 inputs utilize data points that are observable, such as quoted prices, interest rates, and yield curves.

As of June 30, 2016, the alternative investments consisted of subscription partnership agreements with capital commitments of approximately $1.9 million, which are subject to periodic distributions. These alternative investments are valued at fair value using NAV or equivalent as determined by the General Partner in the absence of readily ascertainable market values. Distributions under this investment structure are made to investors through the liquidation of the underlying assets. All assets are unable to be fully distributed to the limited partners until the dissolution of the partnership, which may not be until a point in the future. The fair value of limited partnership interests is generally based on fair value capital balances reported by the underlying partnerships, subject to management review and adjustment. Security values of companies traded on exchanges, or quoted on NASDAQ, are based upon the last reported sales price on the valuation date. Security values of companies traded over the counter, but not quoted on NASDAQ, and securities for which no sale occurred on the valuation date are based upon the last quoted bid price. The value of any security for which a market quotation is not readily available may be its cost, provided however, that the General Partner adjusts such cost value to reflect any bona fide third party transactions in such a security between knowledgeable investors, of which the General Partner has knowledge. In the absence of any such third party transactions, the General Partner may use other information to develop a good faith determination of value. Examples include, but are not limited to, discounted cash flow models, absolute value models, and price multiple models. Inputs for these models may include, but are not limited to, financial statement information, discount rates, and salvage value assumptions.

(In thousands)

As of June 30, 2016 and 2015, the Level 3 investments consist of $232 and $258, respectively, of preferred shares in a private equity fund. The private equity fund is a part of the permanently restricted trust in which Joseph Richey holds an economic interest and were recorded pursuant to the acquisition of Joseph Richey and the consolidation of its financial statements. The shares are valued at their fixed redemption value. There were no significant transfers between levels during the years ended June 30, 2016 and 2015.

Fair value of the fixed assets acquired in the acquisition of Richey was determined using a market comparable technique, which is considered a Level 3 valuation technique.

Investments and limited or restricted use funds comprise of the following uses and purposes at June 30:

| | | 2016 | 2015 |
|---|---|---|---|
| Insurance settlements | $ | 424 | 476 |
| Donor restricted | | 19,281 | 19,672 |
| Unrestricted | | 62,499 | 61,937 |
| | $ | 82,204 | 82,085 |

(In thousands)

Investment income and gains (losses) for cash and cash equivalents and investments and limited use funds comprise of the following for the years ended June 30:

| | | 2016 | 2015 |
|---|---|---|---|
| Unrestricted income (loss): | | | |
| Dividends and interest, net | $ | 1,366 | 1,344 |
| Realized gains on sales of investments | | 1,650 | 3,131 |
| Unrealized losses on investments | | (3,467) | (1,567) |
| Total unrestricted (loss) income, net | $ | (451) | 2,908 |
| Temporarily restricted income (loss): | | | |
| Dividends and interest, net | $ | 272 | 169 |
| Realized gains on sales of investments | | 375 | 939 |
| Unrealized losses on investments | | (1,061) | (1,084) |
| Total temporarily restricted (loss) income, net | $ | (414) | 24 |
| Permanently restricted income (loss): | | | |
| Unrealized losses on investments | $ | (111) | (89) |
| Total permanently restricted loss, net | $ | (111) | (89) |

## (5) Property, Plant, and Equipment

Property, plant, and equipment as of June 30 consisted of the following:

| | | 2016 | 2015 |
|---|---|---|---|
| Land and land improvements | $ | 114 | 114 |
| Buildings and building service equipment | | 18,401 | 17,087 |
| Leasehold improvements | | 192 | 96 |
| Office furniture and equipment | | 5,591 | 7,286 |
| | | 24,298 | 24,583 |
| Less accumulated depreciation and amortization | | (11,607) | (12,380) |
| Total property, plant and equipment, net | $ | 12,691 | 12,203 |
| Depreciation expense | $ | 1,358 | 1,268 |

(In thousands)

## (6) Long-Term Debt

Long-term debt as of June 30 consisted of the following:

| | | 2016 | 2015 |
|---|---|---|---|
| M&T mortgage note – 5.5% | $ | — | 830 |
| M&T line of credit – 4.0% | | — | 436 |
| | | — | 1,266 |
| Less current portion of long-term debt | | — | (489) |
| | $ | — | 777 |

On December 13, 2015, the Company repaid the mortgage payable and line of credit, which were assumed in connection with the acquisition of Richey.

## (7) Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets available for the following purposes and amounts released as of and for the years ended June 30 were as follows:

| | | Available balance | | Released | |
|---|---|---|---|---|---|
| | | 2016 | 2015 | 2016 | 2015 |
| Charity and uncompensated care | $ | 2,739 | 4,266 | 985 | 1,146 |
| Jewish Hospice Program | | 2,697 | — | — | — |
| Departmental needs | | 1,024 | 1,069 | 1,869 | 1,824 |
| Gilchrist Kids | | 948 | 1,120 | 370 | 437 |
| Time Restriction | | 561 | 586 | — | — |
| Joseph Richey | | 423 | 33 | 323 | 112 |
| Total temporarily restricted net assets | $ | 8,392 | 7,074 | 3,547 | 3,519 |

(In thousands)

Permanently restricted net assets as of June 30, 2016 and 2015 are restricted to the following:

| | | 2016 | 2015 |
|---|---|---|---|
| Endowment for charity and uncompensated care | $ | 10,068 | 10,067 |
| Joseph Richey endowment | | 2,133 | 2,246 |
| Gilchrist kids endowment | | 1,885 | 1,869 |
| Jewish Hospice Program | | 125 | — |
| Total permanently restricted net assets | $ | 14,211 | 14,182 |

The Hospice's endowment fund consists of a $10 million endowment for charity and uncompensated care, as well as other donations from individual donors. Earnings on the endowment for charity and uncompensated care are temporarily restricted for such purposes.

During fiscal year 2012, the Board of Directors of the Hospice established the Gilchrist Kids endowment with an initial goal of raising $5 million.

The Hospice has no internal board-designated endowment funds recorded in unrestricted net assets. The net assets associated with endowment are classified and reported based on the existence or absence of donor-imposed restrictions.

The Hospice has interpreted the "Uniform Prudent Management of Institutional Funds Act" (UPMIFA) as requiring the preservation of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Hospice classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure of the Hospice in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Hospice considers the following factors in making a determination to appropriate or accumulate endowment funds:

- The duration and preservation of the fund
- The purposes of the Hospice and the donor-restricted endowment fund
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of the organization
- The investment policies of the organization

(In thousands)

The Hospice had the following activities to its endowment fund during the years ended June 30, 2016 and 2015, delineated by net asset class:

| | Unrestricted | Temporary restricted | Permanently restricted | Total |
|---|---|---|---|---|
| Endowment net assets, June 30, 2014 | $ — | 4,907 | 11,663 | 16,570 |
| Investment return: | | | | |
| Investment income, net | — | 327 | — | 327 |
| Net appreciation (realized and unrealized) | — | 100 | (89) | 11 |
| Total investment return | — | 427 | (89) | 338 |
| Inherent contribution | — | — | 2,322 | 2,322 |
| Contributions | — | — | 286 | 286 |
| Appropriation of endowment assets for expenditure | — | (1,145) | — | (1,145) |
| Endowment net assets, June 30, 2015 | $ — | 4,189 | 14,182 | 18,371 |
| Investment return: | | | | |
| Investment income, net | $ — | 296 | — | 296 |
| Net appreciation (realized and unrealized) | — | (689) | (111) | (800) |
| Total investment return | — | (393) | (111) | (504) |
| Contributions | — | — | 140 | 140 |
| Appropriation of endowment assets for expenditure | — | (1,081) | — | (1,081) |
| Endowment net assets, June 30, 2016 | $ — | 2,715 | 14,211 | 16,926 |

### *(a) Endowment Funds with Deficits*

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the value of the initial and subsequent donor gift amounts (deficit). When donor endowment deficits exist, they are classified as a reduction of unrestricted net assets. As of June 30, 2016, there was one endowment with a deficit that was insignificant. There were no deficits as of June 30, 2015.

### *(b) Return Objectives and Risk Parameters*

The Hospice has adopted endowment investment and spending policies that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of endowment assets. Under this policy, the return objective for the endowment assets, measured over a full market cycle, shall be to maximize the return against a blended index, based on the endowment's target allocation applied to the appropriate individual benchmarks. The Hospice expects its endowment funds over time to provide an average rate of return of approximately 7.5% annually. Actual returns in any given year may vary from this amount.

(In thousands)

### *(c) Strategies Employed for Achieving Investment Objectives*

To achieve its long-term rate of return objectives, the Hospice relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized gains) and current yield (interest and dividends). The Hospice targets a diversified asset allocation that places greater emphasis on equity-based investments to achieve its long-term objectives within prudent risk constraints.

### *(d) Endowment Spending Allocation and Relationship of Spending Policy to Investment Objectives*

The board of directors of the Hospice approves the method to be used to appropriate endowment funds for expenditure. The Hospice is in the process of amending its endowment spending allocation policy to conform to UPMIFA, which was passed by Maryland on April 14, 2009 and limits annual endowment spending to 7.0% of the annual market value per year.

## (8) Related Parties and Affiliates

Advances from affiliates as of June 30, 2016 and 2015 amounted to a payable of $762 and $932, respectively, which were repaid in July 2016 and July 2015, respectively. Advances were noninterest bearing and did not have a stated maturity date.

## (9) Functional Expenses

The Hospice provides hospice services to residents within its service area. Expenses related to providing these services for the years ended June 30, 2016 and 2015 were as follows:

| | | 2016 | 2015 |
|---|---|---|---|
| Healthcare services | $ | 34,834 | 31,343 |
| General and administrative | | 12,404 | 10,934 |
| Total operating expenses | $ | 47,238 | 42,277 |

## (10) Leases

Hospice leases office space in privately owned buildings under leases ranging up to ten years. Options to renew these leases range from five to ten years. Renewal options are not included in the minimum future rental.

(In thousands)

Minimum future rental expenses for the years subsequent to June 30 are as follows:

| | | Rent |
|---|---|---|
| 2017 | $ | 854 |
| 2018 | | 768 |
| 2019 | | 313 |
| 2020 | | 320 |
| | $ | 2,255 |

Rental expenses associated with the facility leases amounted to approximately $814 and $808 for the years ended June 30, 2016 and 2015, respectively.

## (11) Promises to Contribute

The Hospice has received unconditional and conditional promises to give. The pledges receivable are recorded at their present value using a discount rate of 4.0%. The Hospice has two irrevocable trusts whose present value as of June 30, 2016 and 2015 is $461 and $487, respectively. The trusts are recorded as long-term pledge receivables, due over 5 years.

| | | 2016 | 2015 |
|---|---|---|---|
| Due within 1 year | $ | 1,238 | 500 |
| Due 1-5 years | | 1,837 | 727 |
| Due over 5 years | | 461 | 487 |
| Gross pledge receivables | | 3,536 | 1,714 |
| Less discount and allowances | | (214) | (130) |
| Net pledge receivables | $ | 3,322 | 1,584 |

## (12) Subsequent Events

Hospice has evaluated all events and transactions that occurred after June 30, 2016 and through October 6, 2016, the date the financial statements were issued. Hospice did not have any material recognizable subsequent events during the period.

# CONSOLIDATING INFORMATION

Schedule 1

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

Consolidating Balance Sheet

June 30, 2016

(In thousands)

| Assets | Gilchrist Hospice Care Inc. | Joseph Richey House, Inc. | Brownlow Byron Home, Inc. | Eliminating entries | Total |
|---|---|---|---|---|---|
| Current assets: | | | | | |
| Cash and cash equivalents | $ 10,322 | 190 | 113 | — | 10,625 |
| Limited or restricted use funds | 2,460 | — | — | — | 2,460 |
| Patient accounts receivable, net | 5,725 | 207 | — | — | 5,932 |
| Other receivables | 530 | 19 | — | — | 549 |
| Pledge receivables | 1,138 | 100 | — | — | 1,238 |
| Advances to affiliates | 4,715 | 562 | — | (5,277) | — |
| Inventories and other current assets | 106 | 8 | — | — | 114 |
| Total current assets | 24,996 | 1,086 | 113 | (5,277) | 20,918 |
| Investments and limited use funds | 77,674 | 2,070 | — | — | 79,744 |
| Property and equipment, net | 8,768 | 3,667 | 256 | — | 12,691 |
| Pledge accounts receivable | 1,809 | 275 | — | — | 2,084 |
| Other noncurrent assets | 284 | — | — | — | 284 |
| Total assets | $ 113,531 | 7,098 | 369 | (5,277) | 115,721 |
| **Liabilities and Net Assets** | | | | | |
| Current liabilities: | | | | | |
| Accounts payable and accrued expenses | $ 5,170 | 3 | 1 | — | 5,174 |
| Insurance reserves current | 150 | — | — | — | 150 |
| Payable to affiliates | 704 | 4,763 | 572 | (5,277) | 762 |
| Other current liabilities | 457 | 21 | — | — | 478 |
| Total current liabilities | 6,481 | 4,787 | 573 | (5,277) | 6,564 |
| Insurance reserves | 274 | — | — | — | 274 |
| Other long-term liabilities | — | — | 615 | — | 615 |
| Total liabilities | 6,755 | 4,787 | 1,188 | (5,277) | 7,453 |
| Net assets: | | | | | |
| Unrestricted-controlling | 86,733 | (249) | (819) | — | 85,665 |
| Temporarily restricted | 7,965 | 427 | — | — | 8,392 |
| Permanently restricted | 12,078 | 2,133 | — | — | 14,211 |
| | 106,776 | 2,311 | (819) | — | 108,268 |
| Total liabilities and net assets | $ 113,531 | 7,098 | 369 | (5,277) | 115,721 |

See accompanying independent auditors' report.

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

Consolidating Statement of Operations and Changes in Net Assets

June 30, 2016

(In thousands)

| | | Gilchrist Hospice Care Inc. | Joseph Richey House, Inc. | Brownlow Byron Home, Inc. | Eliminating entries | Total |
|---|---|---|---|---|---|---|
| Operating revenues: | | | | | | |
| Patient service revenue net of contractual allowances | $ | 47,268 | 1,112 | — | — | 48,380 |
| Provision for uncollectible accounts | | (1,600) | (56) | — | — | (1,656) |
| Net patient service revenue | | 45,668 | 1,056 | — | — | 46,724 |
| Other operating revenue | | 163 | 118 | 65 | (189) | 157 |
| Net assets released from restrictions | | 3,224 | 323 | — | — | 3,547 |
| Total operating revenue | | 49,055 | 1,497 | 65 | (189) | 50,428 |
| Operating expenses: | | | | | | |
| Salaries, wages and employee benefits | | 31,009 | 1,924 | 89 | — | 33,022 |
| Expendable supplies | | 3,687 | 196 | 6 | — | 3,889 |
| Purchased services | | 8,714 | 365 | 48 | (189) | 8,938 |
| Depreciation and amortization | | 1,172 | 164 | 22 | — | 1,358 |
| Interest | | — | 31 | — | — | 31 |
| Total operating expenses | | 44,582 | 2,680 | 165 | (189) | 47,238 |
| Operating income (loss) | | 4,473 | (1,183) | (100) | — | 3,190 |
| Other income: | | | | | | |
| Contributions | | 680 | 5 | — | — | 685 |
| Fund-raising expense | | (968) | — | — | — | (968) |
| Investment (loss) income, net | | (549) | 98 | — | — | (451) |
| Excess of revenues over expenses | | 3,636 | (1,080) | (100) | — | 2,456 |
| Changes in temporarily restricted net assets: | | | | | | |
| Contributions | | 4,597 | 682 | — | — | 5,279 |
| Investment loss, net | | (414) | — | — | — | (414) |
| Net assets released for operations | | (3,224) | (323) | — | — | (3,547) |
| Increase in temporarily restricted net assets | | 959 | 359 | — | — | 1,318 |
| Changes in permanently restricted net assets: | | | | | | |
| Contributions | | 140 | — | — | — | 140 |
| Investment loss, net | | (11) | (100) | — | — | (111) |
| Increase (decrease) in permanently restricted net assets | | 129 | (100) | — | — | 29 |
| Increase (decrease) in net assets | | 4,724 | (821) | (100) | — | 3,803 |
| Net assets, beginning of year | | 104,465 | — | — | — | 104,465 |
| Net assets, end of year | $ | 109,189 | (821) | (100) | — | 108,268 |

See accompanying independent auditors' report.

KPMG

# GILCHRIST HOSPICE CARE, INC.
# AND SUBSIDIARIES
# D/B/A GILCHRIST SERVICES, INC.

Consolidated Financial Statements
and Consolidating Information

June 30, 2017 and 2016

(With Independent Auditors' Report Thereon)

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

**Table of Contents**

KPMG LLP
1 East Pratt Street
Baltimore, MD 21202-1128

# Independent Auditors' Report

The Board of Directors
Gilchrist Hospice Care, Inc.:

We have audited the accompanying consolidated financial statements of Gilchrist Hospice Care, Inc. and its subsidiaries d/b/a Gilchrist Services, Inc. (the Hospice), which comprise the consolidated balance sheets as of June 30, 2017 and 2016, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended, and the related notes to the consolidated financial statements.

## Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

## Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

## Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Gilchrist Hospice Care, Inc. and its subsidiaries d/b/a Gilchrist Services, Inc. as of June 30, 2017 and 2016, and the results of their operations and their cash flows for the years then ended in accordance with U.S. generally accepted accounting principles.

KPMG

**Other Matter**

Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements as a whole. The accompanying supplementary information in Schedules 1–2 is presented for purposes of additional analysis and is not a required part of the consolidated financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the consolidated financial statements. The information has been subjected to the auditing procedures applied in the audit of the consolidated financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the consolidated financial statements or to the consolidated financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated financial statements as a whole.

KPMG LLP

October 6, 2017

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

Consolidated Balance Sheets

June 30, 2017 and 2016

(In thousands)

| **Assets** | | **2017** | **2016** |
|---|---|---|---|
| Current assets: | | | |
| Cash and cash equivalents | $ | 6,367 | 10,625 |
| Limited or restricted use funds | | 3,651 | 2,460 |
| Patient accounts receivable, net of reserves of $2,978 and $1,747 | | 7,508 | 5,932 |
| Other receivables | | 475 | 549 |
| Inventories and prepaid expenses | | 134 | 114 |
| Current pledge receivables | | 3,366 | 1,238 |
| Total current assets | | 21,501 | 20,918 |
| Noncurrent assets: | | | |
| Investments and limited or restricted use funds | | 101,401 | 79,744 |
| Pledge receivables, net | | 1,740 | 2,084 |
| Property, plant and equipment, net | | 12,048 | 12,691 |
| Other assets | | 267 | 284 |
| Total noncurrent assets | | 115,456 | 94,803 |
| Total assets | $ | 136,957 | 115,721 |
| **Liabilities and Net Assets** | | | |
| Current liabilities: | | | |
| Accounts payable and accrued expenses | $ | 4,633 | 5,174 |
| Insurance reserves, current | | 150 | 150 |
| Advances from affiliates | | 2,671 | 762 |
| Other current liabilities | | 723 | 478 |
| Total current liabilities | | 8,177 | 6,564 |
| Noncurrent liabilities: | | | |
| Insurance reserves | | 316 | 274 |
| Other long-term liabilities | | 615 | 615 |
| Total liabilities | | 9,108 | 7,453 |
| Net assets: | | | |
| Unrestricted | | 101,407 | 85,665 |
| Temporarily restricted | | 9,928 | 8,392 |
| Permanently restricted | | 16,514 | 14,211 |
| Total net assets | | 127,849 | 108,268 |
| Total liabilities and net assets | $ | 136,957 | 115,721 |

See accompanying notes to consolidated financial statements.

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

Consolidated Statements of Operations

Years ended June 30, 2017 and 2016

(In thousands)

| | | 2017 | 2016 |
|---|---|---|---|
| Patient service revenue: | | | |
| Patient service revenue, net of contractual allowances | $ | 51,690 | 48,380 |
| Provision for uncollectible accounts | | (1,538) | (1,656) |
| Net patient service revenue | | 50,152 | 46,724 |
| Other operating revenue: | | | |
| Other revenue | | 205 | 157 |
| Net assets released from restrictions | | 3,728 | 3,547 |
| Total operating revenue | | 54,085 | 50,428 |
| Operating expenses: | | | |
| Salaries, wages and employee benefits | | 34,416 | 33,022 |
| Expendable supplies | | 3,501 | 3,889 |
| Purchased services | | 10,184 | 8,938 |
| Depreciation | | 1,426 | 1,358 |
| Interest | | — | 31 |
| Total operating expenses | | 49,527 | 47,238 |
| Total operating income | | 4,558 | 3,190 |
| Other income (expense): | | | |
| Contributions | | 2,061 | 685 |
| Fund-raising expense | | (1,182) | (968) |
| Investment income (loss), net | | 10,305 | (451) |
| Total other income (loss) | | 11,184 | (734) |
| Excess of revenues over expenses | $ | 15,742 | 2,456 |

See accompanying notes to consolidated financial statements.

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

Consolidated Statements of Changes in Net Assets

Years ended June 30, 2017 and 2016

(In thousands)

| | | 2017 | 2016 |
|---|---|---|---|
| Excess of revenues over expenses and changes in unrestricted net assets | $ | 15,742 | 2,456 |
| Changes in temporarily restricted net assets: | | | |
| Contributions | | 3,140 | 5,279 |
| Investment income (loss), net | | 2,124 | (414) |
| Net assets released for operations | | (3,728) | (3,547) |
| Increase in temporarily restricted net assets | | 1,536 | 1,318 |
| Changes in permanently restricted net assets: | | | |
| Contributions | | 2,218 | 140 |
| Investment income (loss), net | | 85 | (111) |
| Increase in permanently restricted net assets | | 2,303 | 29 |
| Increase in net assets | | 19,581 | 3,803 |
| Net assets, beginning of year | | 108,268 | 104,465 |
| Net assets, end of year | $ | 127,849 | 108,268 |

See accompanying notes to consolidated financial statements.

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

Consolidated Statements of Cash Flows

Years ended June 30, 2017 and 2016

(In thousands)

| | | 2017 | 2016 |
|---|---|---|---|
| Cash flows from operating activities: | | | |
| Change in net assets | $ | 19,581 | 3,803 |
| Adjustments to reconcile change in net assets to net cash provided by operating activities: | | | |
| Depreciation expense | | 1,426 | 1,358 |
| Provision for uncollectible accounts | | 1,538 | 1,656 |
| Realized/unrealized (gains) loss on investments | | (11,029) | 2,614 |
| Restricted interest income on investments | | (273) | (272) |
| Restricted contributions | | (5,358) | (5,419) |
| Changes in assets and liabilities: | | | |
| (Increase) decrease in patient accounts receivable | | (3,114) | 122 |
| Decrease in other assets | | 71 | 307 |
| (Decrease) increase in accounts payable and accrued expenses | | (254) | 1,154 |
| Net cash provided by operating activities | | 2,588 | 5,323 |
| Cash flows from investing activities: | | | |
| Change in investments and restricted use funds | | (11,546) | (2,461) |
| Additions to property and equipment | | (783) | (1,846) |
| Net cash used in investing activities | | (12,329) | (4,307) |
| Cash flows from financing activities: | | | |
| Payment on long-term debt | | — | (1,266) |
| Transfer from (to) affiliates | | 1,909 | (170) |
| Proceeds from restricted contributions | | 3,574 | 3,681 |
| Net cash provided by financing activities | | 5,483 | 2,245 |
| (Decrease) increase in cash | | (4,258) | 3,261 |
| Cash and cash equivalents, beginning of year | | 10,625 | 7,364 |
| Cash and cash equivalents, end of year | $ | 6,367 | 10,625 |
| Cash paid for interest | $ | — | 23 |

See accompanying notes to consolidated financial statements.

## (1) Nature of Operations

Gilchrist Hospice Care, Inc. (the Hospice) is a not-for-profit corporation and a wholly owned subsidiary of GBMC HealthCare, Inc. (the Company). The Hospice, doing business as Gilchrist Services, Inc., provides inpatient and home care hospice services and provides education about hospice care and bereavement services to the public and the healthcare community in Maryland. On October 31, 2014, the Hospice entered into an Affiliation Agreement with Joseph Richey House, Inc. (JRH) and Brownlow Byron Home, Inc. (BBH), collectively referred to as Richey, under which the Hospice became the sole member of JRH and BBH.

JRH is an inpatient hospice residence for terminally ill persons lacking a caregiver in their own homes. JRH has been serving patients in Baltimore City since 1987, providing residential, acute and respite care. JRH is a not-for-profit organization.

BBH is not-for-profit organization that provides elderly and disable persons with housing facilities services in the Richey facility since 1997.

## (2) Summary of Significant Accounting Policies

### *(a) Basis of Accounting*

The accompanying consolidated financial statements have been prepared on the accrual basis of accounting in accordance with U.S. generally accepted accounting principles. Significant intercompany accounts and transactions have been eliminated in consolidation.

### *(b) Cash and Cash Equivalents*

Cash and cash equivalents, carried at cost, which approximates fair value, include amounts invested in accounts that are readily convertible to known amounts of cash with original maturities of three months or less. Cash balances may exceed amounts insured by federal agencies and, therefore, bear a risk of loss. The Hospice has not experienced such losses on these funds to date.

### *(c) Limited Use Funds*

Limited use funds are designated by the donor for a specific use or purpose. Once the donor restrictions have been met, these funds are then released for operations.

### *(d) Investments and Investment Income*

The Hospice investment portfolio is considered a trading portfolio. Investments in marketable securities are measured at fair value. The fair values of the investments are based on quoted market prices or dealer quotes. See note 4 for the discussion of the measurement for fair value for investments.



(Continued)

Alternative investments are recorded under the equity method of accounting. Underlying securities of these alternative investment may include certain debt and equity securities that are not readily marketable. Because certain investments are not readily marketable, their fair value is subject to additional uncertainty, and therefore, values realized upon disposition may vary significantly from current reported values.

Investment income or loss (including realized gains and losses on investments, interest, and dividends) is included in excess of revenues over expenses unless the income or loss is restricted by the donor or law. Investment income on investments of temporarily restricted or permanently restricted net assets is recorded as an increase or decrease in temporarily restricted net assets to the extent restricted by the donor or law.

Investment income is recorded on the accrual basis. Purchases and sales of investments are reflected on a trade-date basis. Realized gains and losses on sales of investments are based on historical cost.

In May 2005, the Hospice received an unrestricted contribution of approximately $25 million to support the ongoing activities of the Hospice. The board of directors of the Hospice has internally designated the contribution for future use.

### *(e) Allowance for Uncollectible Accounts*

Patient accounts receivable are reduced by allowances for uncollectible accounts. In evaluating the collectibility of accounts receivable, the Hospice analyzes historical collections and write-offs and identifies trends for each of its major payor sources of revenue to estimate the appropriate allowance for bad debts and provision for uncollectible accounts. Management regularly reviews its estimate and evaluates the sufficiency of the allowance for uncollectible accounts. The Hospice analyzes contractual amounts due from patients who have third-party coverage and provides an allowance for doubtful accounts and a provision for bad debts. For patient accounts receivable associated with self-pay patients, which includes those patients without insurance coverage exists for a portion of the bill, the Hospice records a significant provision for bad debts for patients that are unable or unwilling to pay for the portion of the bill representing their financial responsibility. Account balances are charged off against the allowance for doubtful accounts after all means of collection have been exhausted.

Hospice allowance for doubtful accounts increased from 23% to 28% of gross accounts receivable from June 30, 2016 to June 30, 2017. During 2017, the Hospice implemented a new electronic medical record and billing system and as a result, management determined additional reserves were necessary.

(In thousands)

The activity in the allowance for bad debts is summarized as follows for the fiscal years ended June 30:

| | | 2017 | 2016 |
|---|---|---|---|
| Beginning balance | $ | 1,747 | 2,956 |
| Provision for uncollectible accounts | | 1,538 | 1,656 |
| Less write offs | | (307) | (2,865) |
| Ending balance | $ | 2,978 | 1,747 |

### *(f) Ground Lease*

Ground lease represents the prepayment to Sheppard Pratt Health System for the lease of land used by the Hospice for its inpatient building. The ground lease is being amortized over 40 years, through March 2033, which is the life of the lease. Ground lease expense was $16 for the years ended June 30, 2017 and 2016, and is recorded as purchased services on the consolidated statements of operations. Ground lease prepayments are included in other assets on the consolidated balance sheets.

### *(g) Property, Plant and Equipment*

Property, plant, and equipment are recorded at cost. Depreciation is computed using the straight-line method over the estimated useful lives of the assets, which range from 3 to 36 years. The cost and accumulated depreciation relating to property, plant, and equipment sold or retired are removed from the respective accounts at the time of disposition and the resulting gain or loss is reflected in the consolidated statements of operations.

### *(h) Other Long-Term Liabilities*

Other long-term liabilities consist of a capital advance in the amount of $615 from the U.S. Department of Housing and Urban Development (HUD). The capital advance does not bear any interest and is not required to be repaid as long as the housing remains available to eligible low-income households for a period of 40 years, expiring in 2040, and functions in accordance with Section 811.

### *(i) Donor-Restricted Gifts*

Unconditional promises to give cash and other assets to the Hospice are reported at their fair value at the date the promise is received. Conditional promises to give and indications of intentions to give are reported at fair value at the date the gift is received. The gifts are reported as either temporarily or permanently restricted if they are received with donor stipulations that limit the use of donated assets. When a donor restriction expires, that is, when a stipulated time restriction ends or purpose of the restriction is accomplished, temporarily restricted net assets are reclassified as unrestricted net assets and reported in the consolidated statements of operations and changes in net assets as net assets released from restrictions. Donor-restricted contributions whose restrictions are met within the same year as received are reported as unrestricted contributions in the accompanying consolidated financial statements.

### (j) *Temporarily and Permanently Restricted Net Assets*

Temporarily restricted net assets are those whose use by the Hospice has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Hospice in perpetuity.

Richey is 1 of 6 named beneficiaries of a charitable trust and receives annual distributions for 50 years, which began in 2005. The distributions are to be used for the unrestricted general charitable purpose of the Richey. After the 50 years, the trust corpus will be distributed to the charities as long as they continue to qualify as a charitable organization under Sections 171(c) and 2055(a) of the Internal Revenue Code. The corpus must be used to create an endowment fund which is permanently restricted and the income should be used for the organization's unrestricted general charitable purpose. The fair value of the trust is included in permanently restricted net assets.

### (k) *Net Patient Service Revenue*

Net patient service revenue is billed on a per-diem basis based on the Medicare fee schedule and contractual agreements for other third-party payors.

### (l) *Excess of Revenues over Expenses*

The consolidated statements of operations include a performance indicator, excess of revenues over expenses. The changes in unrestricted net assets that are excluded from excess of revenues over expenses, consistent with industry practice, include contributions of long-lived assets, including assets acquired using contributions, which by donor restriction were to be used for the purpose of acquiring such assets.

### (m) *Financial Assistance*

As part of the Hospice's mission, it provides hospice care without discrimination on any grounds, including the patients' ability to pay for services. Patients who meet certain criteria under its charity care policy receive free care or services for which the Hospice accepts payments at less than its established rates.

Because the Hospice does not pursue collection of amounts determined to qualify as charity care, they are not reported as revenue. Based on established rates, the Hospice recorded $437 and $340 of charity care in 2017 and 2016, respectively. The total direct and indirect cost of providing the financial assistance was approximately $206 and $221 in 2017 and 2016, respectively.

### (n) *Income Taxes*

The Hospice is a not-for-profit corporation as described in Section 501(c)(3) of the Internal Revenue Code (the Code) and is exempt from federal income taxes on related income pursuant to Section 501(a) of the Code.

The Financial Accounting Standards Board's (FASB) guidance on accounting for uncertainty in income taxes clarifies the accounting for uncertainty of income tax positions. This guidance defines the threshold for recognizing tax return positions in the financial statements as "more likely than not" that the position is sustainable, based on its technical merits. This standard also provides guidance on the measurement, classification and disclosure of tax return positions in the consolidated financial statements. The Hospice has adopted this guidance, and there were no amounts recorded in the consolidated financial statements during the years ended June 30, 2017 and 2016 for uncertain tax positions.

### *(o) Use of Estimates*

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

### *(p) New Accounting Pronouncements*

In 2017, the Hospice adopted ASU No. 2014-15, *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern (Topic 205-40).* This ASU establishes the requirement for management to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued. Management's evaluation should be based on relevant conditions and events that are known and reasonably knowable at the date that the financial statements are issued. Management performed an evaluation as required in this amendment and determined there are no conditions or events that raise substantial doubt about the Hospice's ability to continue as a going concern.

In 2017, the Hospice adopted ASU No. 2015-07, *Fair Value Measurement (Topic 820) Disclosures for Investments in Certain Entities that Calculate Net Asset Value per Share*. This ASU removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient. The amendments also remove the requirement to make certain disclosures for all investments that are eligible to be measured at fair value using the net asset value per share practical expedient. Rather, those disclosures are limited to investments for which the entity has elected to measure the fair value using that practical expedient. This change has been applied retrospectively to July 1, 2015 and was a disclosure only impact. There was no impact on the consolidated balance sheets or statements of operations and changes in net assets.

The FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. This ASU establishes principles for reporting useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from the entity's contracts with customers. Particularly, that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. ASU No. 2014-09 is effective for fiscal year 2019. Hospice does not anticipate that the adoption of this ASU will have a material impact on its financial position or its results of operations.

The FASB issued ASU No. 2016-02, *Leases (Topic 842),* which will require lessees to recognize most leases on-balance sheet, which will increase their reported assets and liabilities. The adoption of ASU No. 2016-02 is effective in fiscal year 2020, and will require application of the new guidance at the beginning of the earliest comparable period presented. Early adoption is permitted. Hospice is currently assessing the impact of the adoption of ASU No. 2016-02 which is expected to increase the Company's assets and liabilities but not have a significant impact on the results of operations.

The FASB issued ASU No. 2016-14, *Not-for-Profit Entities (Topic 958),* which amends the requirements for financial statements and notes in Topic 958, Not-for-Profit Entities (NFP), and requires a NFP to:

- Reduce the number of net asset classes presented from three to two: with donor restrictions and without donor restrictions;
- Present expenses by their functional and their natural classifications in one location in the financial statements;
- Provide quantitative and qualitative information about management of liquid resources and availability of financial assets to meet cash needs within one year of the balance sheet date.

The adoption of ASU No. 2016-14 is effective in fiscal year 2019, and is applied retrospectively in the year of adoption. Hospice does not anticipate that the adoption of this ASU will have a material impact on its financial position and results of operations.

(In thousands)

### (3) Concentrations of Credit Risk

The Hospice grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of patient service revenue and patient accounts receivable from third parties as of and for the years ended June 30 is as follows:

| | Accounts receivable | | Revenue | |
|---|---|---|---|---|
| | 2017 | 2016 | 2017 | 2016 |
| Medicare | 80 % | 66 % | 86 % | 86 % |
| Medicaid | 5 | 4 | 3 | 3 |
| Blue cross | 3 | 6 | 3 | 1 |
| Commercial managed care entities | 4 | 8 | 4 | 6 |
| Other third party payors | 8 | 16 | 4 | 4 |
| Total | 100 % | 100 % | 100 % | 100 % |

The Hospice provides hospice services in the state of Maryland. The Hospice and other healthcare providers are subject to certain inherent risks, including: dependence on revenue derived from reimbursement by the federal Medicare and state Medicaid programs, and government regulation, government budgetary constraints, and proposed legislative and regulatory changes.

The Medicare and state Medicaid reimbursement programs represent a substantial portion of the Hospice's revenues and the Hospice's operations are subject to a variety of other federal, state, and local regulatory requirements. Failure to maintain required regulatory approvals and licenses and/or changes in such regulatory requirements could have a significant adverse effect on the Hospice. Changes in federal and state reimbursement funding mechanisms and related government budgetary constraints could have a significant adverse effect on the Hospice.

As a result of recently enacted and pending federal healthcare reform legislation, substantial changes are anticipated in the U.S. healthcare system. Such legislation includes numerous provisions affecting the delivery of healthcare services, the financing of healthcare costs, reimbursement to healthcare providers, and the legal obligations of health insurers, providers, and employers. These provisions are currently slated to take effect at specified times over the next decade. This federal healthcare reform legislation did not affect the 2017 and 2016 consolidated financial statements.

Additional Documentation Requests (ADR) began in December 2009 to perform prepayment reviews of claims targeted to those services with the highest improper payments. ADR reviews at the Hospice covered areas of beneficiary election statement, certification, plans of care and eligibility.



(Continued)

## (4) Investments and Limited Use Funds

Guidance for fair value measurements establishes a hierarchy of valuation inputs based on the extent to which the inputs are observable in the marketplace. Observable inputs reflect market data obtained from sources independent of the reporting entity and unobservable inputs reflect the entities own assumptions about how market participants would value an asset or liability based on the best information available. Valuation techniques used to measure fair value under current guidance must maximize the use of observable inputs and minimize the use of unobservable inputs. The guidance describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the last unobservable, that may be used to measure fair value.

The following describes the hierarchy of inputs used to measure fair value and the primary valuation methodologies used by the Hospice for financial instruments measured at fair value on a recurring basis. The three levels of inputs are as follows:

- Level 1 – Quoted prices in active markets for identical assets or liabilities
- Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the same term of the assets or liabilities
- Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities

(In thousands)

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. The tables below present the balances of assets measured at fair value by level, excluding alternative investments in the amount of $1,171 and $356, which are accounted for under the equity method, as of June 30, 2017 and 2016, respectively:

| | June 30, 2017 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| Managed cash funds | $ 9,798 | — | — | 9,798 |
| Common stock | 48,638 | — | — | 48,638 |
| Foreign stock | 3,536 | — | — | 3,536 |
| Mutual funds | 11,993 | — | — | 11,993 |
| Total equity | 64,167 | — | — | 64,167 |
| Bonds – fixed income | — | 363 | — | 363 |
| Bonds – fixed income international | — | 51 | — | 51 |
| Mutual funds – fixed income | — | 29,385 | — | 29,385 |
| Municipal bonds | — | 117 | — | 117 |
| Total fixed income | — | 29,916 | — | 29,916 |
| Total investment and limited or restricted use funds | 73,965 | 29,916 | — | 103,881 |
| Less current portion | 3,651 | — | — | 3,651 |
| Total noncurrent investment and limited or restricted use funds | $ 70,314 | 29,916 | — | 100,230 |

(In thousands)

| | June 30, 2016 | | | |
|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total |
| Managed cash funds | $ 4,035 | — | — | 4,035 |
| Common stock | 39,299 | 58 | 232 | 39,589 |
| Foreign stock | 3,241 | — | — | 3,241 |
| Mutual funds | 9,135 | — | — | 9,135 |
| Total equity | 51,675 | 58 | 232 | 51,965 |
| Corporate debt securities | — | 2,455 | — | 2,455 |
| Bonds – U.S. Treasury | 134 | — | — | 134 |
| Bonds – federal agency backed | — | 96 | — | 96 |
| Bonds – fixed income | — | 474 | — | 474 |
| Bonds – fixed income international | — | 52 | — | 52 |
| Mutual funds – fixed income | — | 22,511 | — | 22,511 |
| Municipal bonds | — | 126 | — | 126 |
| Total fixed income | 134 | 25,714 | — | 25,848 |
| Total investment and limited or restricted use funds | 55,844 | 25,772 | 232 | 81,848 |
| Less current portion | 2,460 | — | — | 2,460 |
| Total noncurrent investment and limited or restricted use funds | $ 53,384 | 25,772 | 232 | 79,388 |

Hospice values Level 1 marketable securities using the closing market prices as of the valuation date. Fair values determined by Level 1 inputs utilize quoted trades at least weekly in an active market. The Hospice values Level 2 investments using the current prices published. Fair values determined by Level 2 inputs utilize data points that are observable, such as quoted prices, interest rates, and yield curves.

As of June 30, 2017 and 2016, the alternative investments consisted of subscription partnership agreements with capital commitments of approximately $1.9 million which are subject to periodic distributions. These alternative investments are valued at fair value using Net Asset Value or equivalent as determined by the General Partner in the absence of readily ascertainable market values. Distributions under this investment structure are made to investors through the liquidation of the underlying assets. All assets are unable to be fully distributed to the limited partners until the dissolution of the partnership, which may not be until a point in the future. The fair value of limited partnership interests is generally based on fair value capital balances reported by the underlying partnerships, subject to management review and adjustment. Security values of companies traded on exchanges, or quoted on NASDAQ, are based upon the last reported sales price on the valuation date. Security values of companies traded over the counter, but not quoted on NASDAQ, and securities for which no sale occurred on the valuation date are based upon the last quoted bid price. The value of any security for which a market quotation is not readily available may be its cost, provided however, that the General Partner adjusts such cost value to reflect any bona fide third party transactions in such a security between knowledgeable investors, of which the General Partner has knowledge. In the absence of any such third party transactions, the General Partner may use other information to develop a good faith determination of value. Examples include, but are not limited to, discounted cash flow models, absolute value models, and price multiple models. Inputs for these models may include, but are not limited to, financial statement information, discount rates, and salvage value assumptions.

(In thousands)

The investment strategies within the alternative investments include strategies such as middle market growth, private equity, natural resources, and various other asset classes. The investments are subject to restrictions and are not available to be redeemed until certain time restrictions are met, which range from 7 to 10 years with 2 year options extensions.

As of June 30, 2016, the Level 3 investments consist of $232 of preferred shares in a private equity fund. The private equity fund is a part of the permanently restricted trust in which Joseph Richey holds an economic interest and was recorded pursuant to the acquisition of Joseph Richey and the consolidation of its financial statements. The shares are valued at their fixed redemption value and were sold in 2017. There were no other significant transfers between levels during the years ended June 30, 2017 and 2016.

Investments and limited or restricted use funds comprise the following uses and purposes at June 30:

| | | 2017 | 2016 |
|---|---|---|---|
| Insurance settlements | $ | 466 | 424 |
| Donor restricted | | 21,336 | 19,281 |
| Unrestricted | | 83,250 | 62,499 |
| | $ | 105,052 | 82,204 |

(In thousands)

Investment income and gains (losses) for cash and cash equivalents and investments and limited use funds comprise the following for the years ended June 30:

| | | 2017 | 2016 |
|---|---|---|---|
| Unrestricted income (loss): | | | |
| Dividends and interest, net | $ | 1,212 | 1,366 |
| Realized gains on sales of investments | | 2,194 | 1,650 |
| Unrealized gains (losses) on investments | | 6,899 | (3,467) |
| Total unrestricted income (loss), net | | 10,305 | (451) |
| Temporarily restricted income (loss): | | | |
| Dividends and interest, net | | 273 | 272 |
| Realized gains on sales of investments | | 535 | 375 |
| Unrealized gains (losses) on investments | | 1,316 | (1,061) |
| Total temporarily restricted income (loss), net | | 2,124 | (414) |
| Permanently restricted income (loss): | | | |
| Unrealized gains (losses) on investments | | 85 | (111) |
| Total permanently restricted income (loss), net | | 85 | (111) |
| Total investment income (loss) | $ | 12,514 | (976) |

## (5) Property, Plant, and Equipment

Property, plant, and equipment as of June 30 consisted of the following:

| | | 2017 | 2016 |
|---|---|---|---|
| Land and land improvements | $ | 114 | 114 |
| Buildings and building service equipment | | 18,961 | 18,401 |
| Leasehold improvements | | 53 | 192 |
| Office furniture and equipment | | 5,954 | 5,591 |
| | | 25,082 | 24,298 |
| Less accumulated depreciation and amortization | | (13,034) | (11,607) |
| Total property, plant and equipment, net | $ | 12,048 | 12,691 |
| Depreciation expense | $ | 1,426 | 1,358 |

(In thousands)

## (6) Long-Term Debt

On December 13, 2015, the Company repaid the mortgage payable and line of credit, which were assumed in connection with the acquisition of Richey.

## (7) Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets available for the following purposes and amounts released as of and for the years ended June 30 were as follows:

| | | Available balance | | Released | |
|---|---|---|---|---|---|
| | | 2017 | 2016 | 2017 | 2016 |
| Charity and uncompensated care | $ | 3,675 | 2,739 | 887 | 985 |
| Jewish Hospice Program | | 3,376 | 2,697 | — | — |
| Departmental needs | | 1,128 | 1,024 | 2,078 | 1,869 |
| Gilchrist Kids | | 959 | 948 | 200 | 370 |
| Time restriction | | 472 | 561 | 100 | — |
| Joseph Richey | | 318 | 423 | 463 | 323 |
| Total temporarily restricted net assets | $ | 9,928 | 8,392 | 3,728 | 3,547 |

Permanently restricted net assets as of June 30, 2017 and 2016 are restricted to the following:

| | | 2017 | 2016 |
|---|---|---|---|
| Endowment for charity and uncompensated care | $ | 11,380 | 10,068 |
| Joseph Richey endowment | | 2,218 | 2,133 |
| Gilchrist kids endowment | | 2,456 | 1,885 |
| Jewish Hospice Program | | 460 | 125 |
| Total permanently restricted net assets | $ | 16,514 | 14,211 |

The Hospice's endowment fund consists of a $10 million endowment for charity and uncompensated care, as well as other donations from individual donors. Earnings on the endowment for charity and uncompensated care are temporarily restricted for such purposes.

During fiscal year 2012, the Board of Directors of the Hospice established the Gilchrist Kids endowment with an initial goal of raising $5 million.



(Continued)

The Hospice has no internal board-designated endowment funds recorded in unrestricted net assets. The net assets associated with endowment are classified and reported based on the existence or absence of donor-imposed restrictions.

The Hospice has interpreted the "Uniform Prudent Management of Institutional Funds Act" (UPMIFA) as requiring the preservation of the original gift as of the gift date of the donor-restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the Hospice classifies as permanently restricted net assets the original value of gifts donated to the permanent endowment. The remaining portion of the donor-restricted endowment fund that is not classified in permanently restricted net assets is classified as temporarily restricted net assets until those amounts are appropriated for expenditure of the Hospice in a manner consistent with the standard of prudence prescribed by UPMIFA. In accordance with UPMIFA, the Hospice considers the following factors in making a determination to appropriate or accumulate endowment funds:

- The duration and preservation of the fund
- The purposes of the Hospice and the donor-restricted endowment fund
- General economic conditions
- The possible effect of inflation and deflation
- The expected total return from income and the appreciation of investments
- Other resources of the organization
- The investment policies of the organization

(In thousands)

The Hospice had the following activities to its endowment fund during the years ended June 30, 2017 and 2016, delineated by net asset class:

| | Unrestricted | Temporary restricted | Permanently restricted | Total |
|---|---|---|---|---|
| Endowment net assets, June 30, 2015 | $ — | 4,189 | 14,182 | 18,371 |
| Investment return: | | | | |
| Investment income, net | — | 296 | — | 296 |
| Net depreciation (realized and unrealized) | — | (689) | (111) | (800) |
| Total investment return | — | (393) | (111) | (504) |
| Contributions | — | — | 140 | 140 |
| Appropriation of endowment assets for expenditure | — | (1,081) | — | (1,081) |
| Endowment net assets, June 30, 2016 | — | 2,715 | 14,211 | 16,926 |
| Investment return: | | | | |
| Investment income, net | — | 265 | — | 265 |
| Net appreciation (realized and unrealized) | — | 1,859 | 85 | 1,944 |
| Total investment return | — | 2,124 | 85 | 2,209 |
| Contributions | — | | 2,218 | 2,218 |
| Appropriation of endowment assets for expenditure | — | (887) | — | (887) |
| Endowment net assets, June 30, 2017 | $ — | 3,952 | 16,514 | 20,466 |

### *(a) Endowment Funds with Deficits*

From time to time, the fair value of assets associated with individual donor-restricted endowment funds may fall below the value of the initial and subsequent donor gift amounts (deficit). When donor endowment deficits exist, they are classified as a reduction of unrestricted net assets. There were no deficits as of June 30, 2017. As of June 30, 2016, there was one endowment with a deficit that was insignificant.

(In thousands)

### *(b) Return Objectives and Risk Parameters*

The Hospice has adopted endowment investment and spending policies that attempt to provide a predictable stream of funding to programs supported by its endowment while seeking to maintain the purchasing power of endowment assets. Under this policy, the return objective for the endowment assets, measured over a full market cycle, shall be to maximize the return against a blended index, based on the endowment's target allocation applied to the appropriate individual benchmarks. The Hospice expects its endowment funds over time to provide an average rate of return of approximately 7.5% annually. Actual returns in any given year may vary from this amount.

### *(c) Strategies Employed for Achieving Investment Objectives*

To achieve its long-term rate of return objectives, the Hospice relies on a total return strategy in which investment returns are achieved through both capital appreciation (realized and unrealized gains) and current yield (interest and dividends). The Hospice targets a diversified asset allocation that places greater emphasis on equity-based investments to achieve its long-term objectives within prudent risk constraints.

### *(d) Endowment Spending Allocation and Relationship of Spending Policy to Investment Objectives*

The board of directors of the Hospice approves the method to be used to appropriate endowment funds for expenditure. The Hospice is in the process of amending its endowment spending allocation policy to conform to UPMIFA, which was passed by Maryland on April 14, 2009 and limits annual endowment spending to 7.0% of the annual market value per year.

## (8) Related Parties and Affiliates

Advances from affiliates as of June 30, 2017 and 2016 amounted to a payable of $2,671 and $762, respectively, which was repaid in July 2017 and July 2016, respectively. Advances were non-interest-bearing and did not have a stated maturity date.

## (9) Functional Expenses

The Hospice provides hospice services to residents within its service area. Expenses related to providing these services for the years ended June 30, 2017 and 2016 were as follows:

| | | 2017 | 2016 |
|---|---|---|---|
| Healthcare services | $ | 38,249 | 34,834 |
| General and administrative | | 11,278 | 12,404 |
| Total operating expenses | $ | 49,527 | 47,238 |

(In thousands)

## (10) Leases

Hospice leases office space in privately owned buildings under leases ranging up to 10 years through 2020. Options to renew these leases range from 5 to 10 years. Renewal options are not included in the minimum future rental.

Minimum future rental expenses for the years subsequent to June 30 are as follows:

| | | Rent |
|---|---|---|
| 2018 | $ | 768 |
| 2019 | | 313 |
| 2020 | | 320 |
| | $ | 1,401 |

Rental expenses associated with the facility leases amounted to approximately $840 and $814 for the years ended June 30, 2017 and 2016, respectively.

## (11) Promises to Contribute

The Hospice has received unconditional and conditional promises to give. The pledges receivable are recorded at their present value using a discount rate of 4.0%. The Hospice has two irrevocable trusts whose present value as of June 30, 2017 and 2016 is $469 and $461, respectively. The trusts are recorded as long-term pledge receivables, due over 5 years.

| | | 2017 | 2016 |
|---|---|---|---|
| Due within 1 year | $ | 3,366 | 1,238 |
| Due 1-5 years | | 1,460 | 1,837 |
| Due over 5 years | | 469 | 461 |
| Gross pledge receivables | | 5,295 | 3,536 |
| Less discount and allowances | | (189) | (214) |
| Net pledge receivables | $ | 5,106 | 3,322 |

## (12) Subsequent Events

Hospice has evaluated all events and transactions that occurred after June 30, 2017 and through October 6, 2017 the date the financial statements were issued. Hospice did not have any material recognizable subsequent events during the period.

# CONSOLIDATING INFORMATION

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

Consolidating Balance Sheet

June 30, 2017

(In thousands)

| Assets | Gilchrist Hospice Care Inc. | Joseph Richey House, Inc. | Brownlow Byron Home, Inc. | Eliminating entries | Total |
|---|---|---|---|---|---|
| Current assets: | | | | | |
| Cash and cash equivalents | $ 5,403 | 807 | 157 | — | 6,367 |
| Limited or restricted use funds | 3,651 | — | — | — | 3,651 |
| Patient accounts receivable, net | 7,135 | 373 | — | — | 7,508 |
| Other receivables | 457 | 18 | — | — | 475 |
| Pledge receivables | 3,266 | 100 | — | — | 3,366 |
| Advances to affiliates | 6,220 | 759 | — | (6,979) | — |
| Inventories and other current assets | 129 | 5 | — | — | 134 |
| Total current assets | 26,261 | 2,062 | 157 | (6,979) | 21,501 |
| Investments and limited use funds | 99,245 | 2,156 | — | — | 101,401 |
| Property and equipment, net | 8,307 | 3,509 | 232 | — | 12,048 |
| Pledge accounts receivable | 1,559 | 181 | — | — | 1,740 |
| Other noncurrent assets | 267 | — | — | — | 267 |
| Total assets | $ 135,639 | 7,908 | 389 | (6,979) | 136,957 |
| **Liabilities and Net Assets** | | | | | |
| Current liabilities: | | | | | |
| Accounts payable and accrued expenses | $ 4,632 | — | 1 | — | 4,633 |
| Insurance reserves current | 150 | — | — | — | 150 |
| Payable to affiliates | 2,089 | 6,791 | 770 | (6,979) | 2,671 |
| Other current liabilities | 703 | 20 | — | — | 723 |
| Total current liabilities | 7,574 | 6,811 | 771 | (6,979) | 8,177 |
| Insurance reserves | 316 | — | — | — | 316 |
| Other long-term liabilities | — | — | 615 | — | 615 |
| Total liabilities | 7,890 | 6,811 | 1,386 | (6,979) | 9,108 |
| Net assets: | | | | | |
| Unrestricted-controlling | 103,838 | (1,434) | (997) | — | 101,407 |
| Temporarily restricted | 9,615 | 313 | — | — | 9,928 |
| Permanently restricted | 14,296 | 2,218 | — | — | 16,514 |
| | 127,749 | 1,097 | (997) | — | 127,849 |
| Total liabilities and net assets | $ 135,639 | 7,908 | 389 | (6,979) | 136,957 |

See accompanying independent auditors' report.

**GILCHRIST HOSPICE CARE, INC.**
**AND SUBSIDIARIES**
**D/B/A GILCHRIST SERVICES, INC.**

Consolidating Statement of Operations and Changes in Net Assets

June 30, 2017

(In thousands)

| | Gilchrist Hospice Care Inc. | Joseph Richey House, Inc. | Brownlow Byron Home, Inc. | Eliminating entries | Total |
|---|---|---|---|---|---|
| Operating revenues: | | | | | |
| Patient service revenue net of contractual allowances | $ 50,573 | 1,117 | — | — | 51,690 |
| Provision for uncollectible accounts | (1,434) | (104) | — | — | (1,538) |
| Net patient service revenue | 49,139 | 1,013 | — | — | 50,152 |
| Other operating revenue | 207 | 236 | 66 | (304) | 205 |
| Net assets released from restrictions | 3,265 | 463 | — | — | 3,728 |
| Total operating revenue | 52,611 | 1,712 | 66 | (304) | 54,085 |
| Operating expenses: | | | | | |
| Salaries, wages and employee benefits | 32,148 | 2,092 | 176 | — | 34,416 |
| Expendable supplies | 3,279 | 216 | 6 | — | 3,501 |
| Purchased services | 9,938 | 512 | 38 | (304) | 10,184 |
| Depreciation and amortization | 1,227 | 175 | 24 | — | 1,426 |
| Total operating expenses | 46,592 | 2,995 | 244 | (304) | 49,527 |
| Operating income (loss) | 6,019 | (1,283) | (178) | — | 4,558 |
| Other income: | | | | | |
| Contributions | 2,053 | 8 | — | — | 2,061 |
| Fund-raising expense | (1,182) | — | — | — | (1,182) |
| Investment income, net | 10,215 | 90 | — | — | 10,305 |
| Excess of revenues over expenses | 17,105 | (1,185) | (178) | — | 15,742 |
| Changes in temporarily restricted net assets: | | | | | |
| Contributions | 2,791 | 349 | — | — | 3,140 |
| Investment income, net | 2,124 | — | — | — | 2,124 |
| Net assets released for operations | (3,265) | (463) | — | — | (3,728) |
| Increase (decrease) in temporarily restricted net assets | 1,650 | (114) | — | — | 1,536 |
| Changes in permanently restricted net assets: | | | | | |
| Contributions | 2,218 | — | — | — | 2,218 |
| Investment income, net | — | 85 | — | — | 85 |
| Increase in permanently restricted net assets | 2,218 | 85 | — | — | 2,303 |
| Increase (decrease) in net assets | 20,973 | (1,214) | (178) | — | 19,581 |
| Net assets, beginning of year | 109,189 | (821) | (100) | — | 108,268 |
| Net assets, end of year | $ 130,162 | (2,035) | (278) | — | 127,849 |

See accompanying independent auditors' report.